Economic Trends

The recovery in Alberta's economy is firmly underway, although momentum is slowing. Strong growth in oil production following the spring outages is boosting the volume of Alberta's energy exports, while the manufacturing sector is getting a lift from the recovery in durable goods. Although the jobs recovery paused in the third quarter, gains in goods sector and full-time employment have bolstered wages in recent months. Momentum in residential construction has also picked up. This month's InFocus looks at how the economic downturn has affected various segments of the Alberta housing market.

Key Indicators

Seasonally adjusted unless otherwise indicated.

Indicator	Latest Month	Value	Change year-over-year (y/y)
Alberta Activity Index (y/y growth)	August	+5.6%	+9.9 p.p.
Employment (thousands)	September	2,279	+0.4%
Unemployment Rate	September	7.9%	-0.8 p.p.
CPI Inflation (unadjusted)	September	1.3%	+0.8 p.p.
Retail Sales	August	$6.7 B	+8.2%
Housing Starts (annualized)	September	29,768	+2.0%
Rigs Drilling (unadjusted)	September	127	+59.7%
Manufacturing Shipments	August	$5.8 B	+9.0%
Exports (unadjusted)	August	$8.1 B	+15.2%

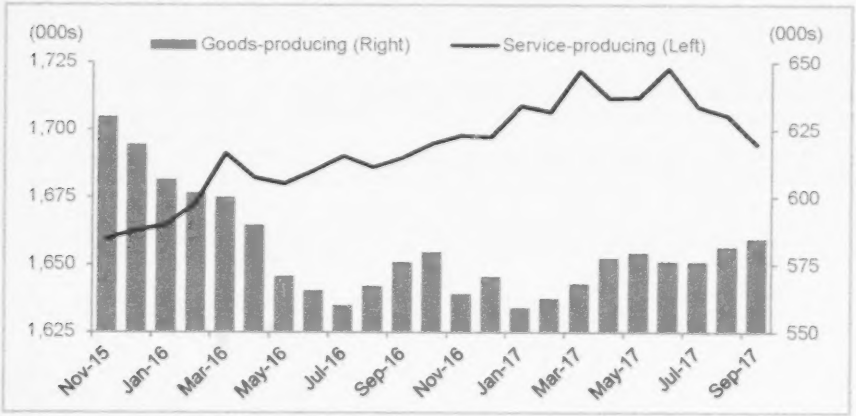
Source: Alberta Treasury Board and Finance, Statistics Canada, CAODC, CMHC.
p.p.= percentage points.

Household Sector

Pullback in service sector jobs

The jobs recovery took a step back in the third quarter. Employment fell by almost 20,000 after increasing by over 31,000 in the first six months of 2017. It was weighed down by the service sector, which lost about 28,000 jobs following six consecutive quarterly gains (Chart 1). The decline was concentrated in education, health care and social assistance, and accommodation and food services, where employment retreated from recent highs. In contrast, goods sector employment advanced by over 8,000 in the third quarter to reach the highest level since April 2016 (Chart 1), reflecting gains in the construction and mining and oil and gas sectors. With the job losses entirely in the service sector, part-time positions fell in the third quarter while full-time positions continued to grow since the beginning of the year.

Chart 1: Service sector employment retreats from all-time high
Alberta employment by industry



Source: Statistics Canada

Goods sector boosts wages

With continued job gains in the goods sector and full-time positions, wages have started to improve. After a sluggish first half of the year, the average hourly wage rate grew 2.8% to reach $30.37/hour in September. Wages have been bolstered by more hiring in high-paying, full-time jobs in the goods sector and wage gains in high-paying industries such as mining and oil and gas, construction, and professional and scientific services. Both the goods and service sectors have seen year-over-year gains, with twelve of the sixteen subsectors higher than a year ago in September.

Weak consumer inflation

Consumer inflation remains subdued despite an uptick in the last four months. Alberta's inflation moved up from 0.4% in June to 1.3% in September, but remained lower than the national average of 1.6%. The muted inflation reflects a waning contribution of energy and weak core inflation. Core inflation (which excludes food and energy) hit a six-year low in September and has remained below 1% since March. It has eased considerably since the beginning of the year, dampened by falling price of durable goods and

slower growth in service inflation. Price gains in travel and restaurant services have moderated alongside lower prices for vehicle operating cost, communication, home entertainment, rents and homeowners replacement cost.

Other multi-units gaining ground in residential construction

Activity in residential construction continues to advance at a solid pace. Investment in new housing construction rebounded from its January low to reach a twenty-one month high in July. While activity is being led by continued gains in single-detached, momentum in double and row houses has also picked up in recent months. In contrast, investment in apartments remains weak, as elevated inventories of completed and unsold units continue to weigh on activity in this segment.

Business Sector

Oil production boosts export volumes

Oil production in the province is on the rise after production outages and maintenance shutdowns earlier in the spring curtailed output and exports. Oil production rebounded by nearly 15% since April to reach 3.2 million barrels per day in July. Synthetic crude has now recovered to just below levels seen prior to the upgrader outages, while crude bitumen production has ramped up in recent months to hover around record high. Although energy export volumes rebounded, the value of energy exports in August remained 10% lower compared to March, weighed down by lower prices in the summer.

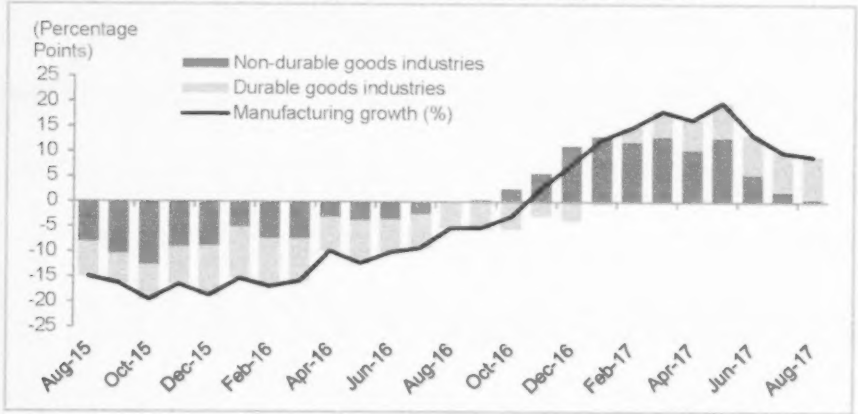
Durable goods buoy shipments

Alberta's manufacturing sector is getting a lift from the recovery in durable goods. Shipments have been supported by a steady rise in durable goods, mainly due to strong gains in wood products and machinery equipment. Improvements in other categories such as fabricated metals, primary metals and non-metallic mineral products have also improved. With most categories gaining ground, the year-over-year growth in durable goods has accelerated (Chart 2). In contrast, the pace of growth in non-durable goods has slowed considerably, dragged down by lower petrochemical volumes and a pullback in chemicals shipments following a spike in fertilizer and pesticide sales in May. Sales of petroleum and coal products have also been easing, although higher prices led to a 1.2% bounce back in overall manufacturing sales in August after easing in the previous two months.

Persistent weakness in Calgary's private sector construction

Investment in Alberta's non-residential building construction continues to flounder. It fell again in the third quarter following a decline in the second quarter. Regionally, the weakness in private sector construction is in Calgary, where investment in commercial and industrial building structures is down 16% year-to-date. This is in contrast to Edmonton where private sector construction spending is up 1% year-to-date, reflecting improvement in industrial investment in the first half of this year. Meanwhile, investment in Alberta's institutional and governmental building construction has started to moderate after ramping up in the last three years.

Chart 2: Durables now contributing more to manufacturing sales growth
Contribution to year-over-year growth in manufacturing shipments



Source: Statistics Canada

Outside Alberta

World economy on the upswing

The International Monetary Fund (IMF) expects global growth to accelerate from 3.2% in 2016 to 3.6% in 2017 and 3.7% in 2018. Global growth is being underpinned by increases in trade, investment, and industrial production, along with improving business and consumer confidence. Growth is also more broad-based, with a notable pick up in the Euro area and Japan, and strong economic activity in emerging Asia and emerging Europe. The IMF noted risks to the outlook, including rising geo-political tensions, tightening global financial conditions, persistently weak inflation in advanced economies, and movement away from regional economic integration.

Slow progress in key trade negotiations

Key trade negotiations have stalled in the last month as negotiating parties are divided over contentious issues. The fourth round of NAFTA renegotiations have ended, with Canada and Mexico rejecting aggressive proposals by the US on auto manufacturing, supply management, dispute-resolution, US public procurement and a NAFTA sunset clause. Similarly, Brexit talks have not progressed on issues regarding EU and UK citizens' rights, the divorce bill and the Northern Ireland border. The outcomes of these negotiations are key risks to the outlook, as protectionist and restrictive policies could potentially undermine the global economic growth.

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inFocus

Home prices stable

After an initial reaction to lower oil prices in 2015, home prices in Alberta have stabilized. However, some segments of the Alberta housing market have been impacted more than others. The price of multi-unit dwellings has fallen more than the price of single unit dwellings, and there has been a bigger impact on housing markets outside of Edmonton and Calgary. This inFocus looks at how the economic downturn has affected various segments of the Alberta housing market.

Home sales declined with oil prices

The drop in oil prices had a profound impact on housing market sentiment. Between November 2014 and February 2015, the number of home resales fell by 28% and the average resale home price fell by 6.2%. Even after the initial declines, resale volumes continued to move in step with changes in the price of oil (Chart 1). This phenomenon was most pronounced in Calgary due to concentration of oil and gas sector. Following the initial adjustment, prices fluctuated but remained relatively steady, with some improvement in 2016. As of September 2017, the average resale price of a home in Alberta was $393,777, up almost 2.7% from the early 2015 low, but 3.7% lower than the peak in 2014.

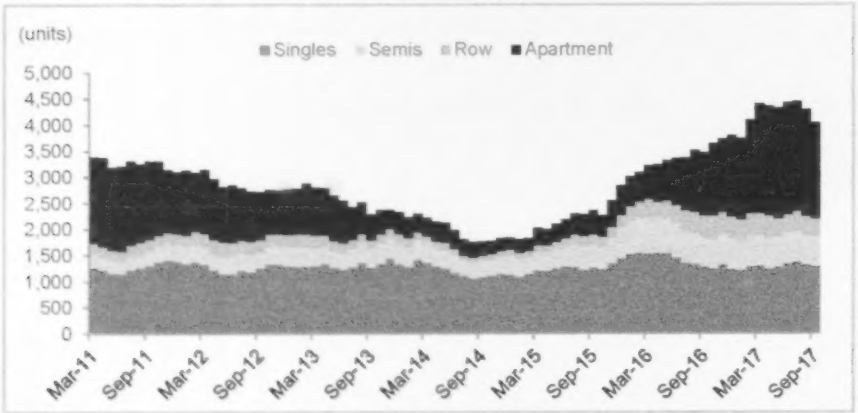
Chart 1: Homes sales fall with the price of oil

Price of West Texas Intermediate (WTI) oil and seasonally adjusted home sales

Source: The Canadian Real Estate Association (CREA), Financial Times

Chart 2: Elevated number of unabsorbed multi-units

Number of completed and unabsorbed units, by type



Source: Canadian Mortgage and Housing Corporation

Prices stable despite weaker fundamentals

Home prices and sales have stabilized at lower levels as economic conditions weakened during the downturn. The unemployment rate, which started to rise in early 2015, climbed to a 22-year high by November 2016. Earnings also declined during the recession, as wages fell and people worked fewer hours. While these weaker demand fundamentals weighed on sales activity, several other factors have helped to keep house prices resilient. The cost of credit has never been lower, with mortgage rates near an all-time low. Even though incomes have fallen, Albertans continue to earn more on average than do residents of other provinces and housing affordability remains reasonable. Though population growth in Alberta slowed, it still outpaced the national growth in both 2015 and 2016.

Some overbuilding in multi-units

Multi-unit construction took a lot longer to respond to changing market conditions. Investment in multi-unit dwellings remained robust until September 2015. This meant that a significant number of projects were being completed just as demand was falling, creating an inventory overhang. The number of completed and unabsorbed apartment units increased throughout 2016 and 2017 (Chart 2), putting persistent downward pressure on apartment prices. In Calgary, these fell by 11.8% between October 2014 and February 2017 before stabilizing.

Surplus supply has also affected the rental market. After falling almost continuously since 1992, the number of purpose-built rental units in the province rebounded dramatically beginning in 2012. This trend was strongest in 2015 and 2016, with the number of rental units growing by over 3% (data for 2017 will not be available until late November). As a result, rental vacancy rates have risen to a 28-year high and rents have been falling more or less continuously since July 2015.

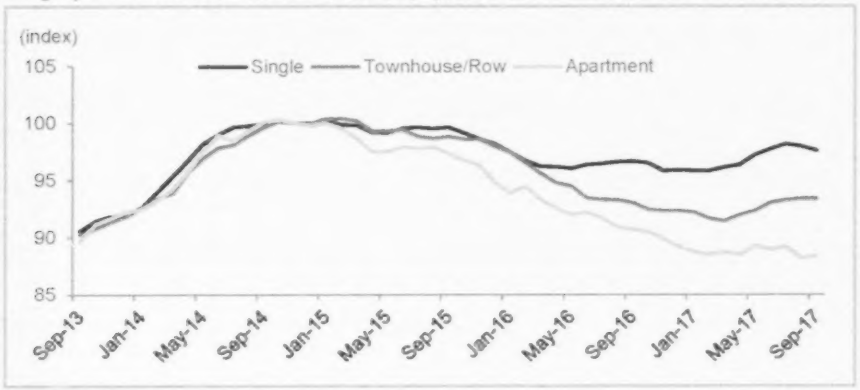
Single-detached a source of stability

In contrast to the supply of multi-unit dwellings, the pace of single-family home building slowed with demand in 2015. As a result, the number of completed and unabsorbed single-family homes has remained near historical levels throughout the recession, in both Calgary and Edmonton. This has helped to support prices for single-family homes (Chart 3). In Calgary, the MLS benchmark price for single-family homes fell far less than the benchmark price for row houses and apartment units.

Since the beginning of 2017, single-unit prices have been rising and are just 2.7% below the January 2015 peak. By contrast, apartment units have not recovered much this year and are 12% below the peak. Since single-family homes make up the majority of the housing market, and on average have higher value, the strength in this sector is a major factor supporting average resale prices in the province. Single-family homes have also been responsible for much of the 21.6% year-to-date increase in housing starts.

Chart 3:Singles a source of stability

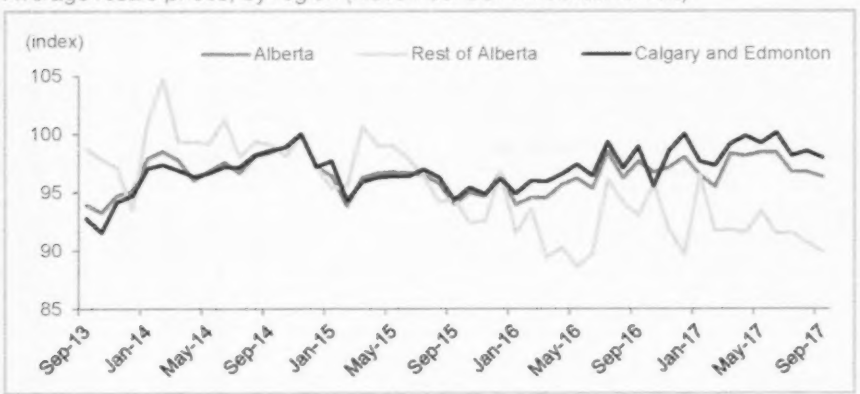
Calgary MLS composite home price, by type (November 2014 indexed to 100)



Source: CREA

Chart 4: Average resale prices steady in major markets

Average resale prices, by region (November 2014 indexed to 100)



Source: CREA

* Change in average resale price using annual data

Disparate regional impacts

The recession had a disproportionately negative impact on markets outside of Edmonton and Calgary (Chart 4). These markets were more exposed to the downturn, with almost half of the province's oil and gas employment located outside the major centres. Employment in this category fell by 56,500 between September 2014 and July 2016, while total employment only fell 34,000 as growth continued in other industries. Consequently, housing markets outside Edmonton and Calgary saw deeper declines and drifted into buyers' markets, while the overall Alberta housing market remained in balance. Prices in these harder hit areas remain well below pre-recession levels in contrast to the two largest centres. Similarly, resale sales volumes are down almost 30%.

Better than past recessions

While home prices have been suppressed by the economic downturn in Alberta, they have held up relatively well compared to previous recessions. The price declines have been more muted compared to both the 1982-83 downturn and the 2009 recession, as demand and supply fundamentals were less affected. The run-up to both of the previous recessions was accompanied with rapid overbuilding. For example, the housing market began correcting in 2007, a full year prior to the 2008-2009 recession. In 2014 by contrast, there were hardly any signs of an overheated market. The resale market has also remained in balance with only a minor increase in the number of listings and foreclosures, while bankruptcies have remained low.

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